

READINESS FINANCE COMMISSION REPORT

I. EXECUTIVE SUMMARY

In June of 2008 Governor Patrick assembled the Readiness Finance Commission and charged it with presenting a variety of alternative means to achieve sustainable education funding for current needs and the sequenced investments necessary for a ten-year Readiness Project implementation plan. The Governor urged the Commission to be bold in its deliberations and to consider all options except raising local property taxes.

Since its formation, the dramatic downturn in our national, state and local economies required the Commission to narrow its focus. The Commission recognized that the state is facing completely different fiscal realities than were contemplated this past summer. The most recent estimates for the fiscal year 2010 budget predict a deficit of between \$2 and \$3 billion dollars. Consequently, early education providers, K-12 school districts and our public institutions of higher education are preparing for a nearly unprecedented reduction in available funding. At the same time, the Commission acknowledged that the economic crisis has highlighted the need to stay committed to a long-term vision of education reform, as outlined in the Readiness Project, as a means to educate a workforce capable of fueling the Massachusetts economy to become a major competitor on a global scale for generations to come.

The Commission's deliberations, therefore, concentrated on the urgent need to find opportunities for cost savings and to maintain support for our education system in a time of inadequate resources. The Commission unequivocally agreed that achieving the vision of the Readiness Project is a worthwhile, indeed vital goal, and that Readiness should be a top priority of both the state and business leaders in order to ensure the future success and competitiveness of the Commonwealth. It was clear that these necessary changes cannot be accomplished with cost-savings alone. Consequently, the Commission recommends a policy package that includes significant and bold restructuring measures to realize cost savings and efficiencies, coupled with new revenues to develop a 21st century education system. Commission members also agreed that, whether they are mandated or incentivized, the cost-savings strategies outlined in this report need to be implemented as soon as possible.

In the Commission's deliberations there was a general sentiment in support of new revenues if attached concretely to efficiencies, restructuring, and tangible savings, and if tied to the next iteration of broad and substantial education reform. Recognizing that savings alone will not be enough even to meet immediate funding needs, several members stressed the need for new revenues now. Though a few members expressed concern about raising revenues during a recession and felt that the state should require implementation of cost-savings measures before looking to new revenues, Commission members strongly believed that the critical role of the education sector warrants support for new, incremental investments, even in this down economy.

While the Commission agrees it is imperative to envision and begin building a 21st century education system as the Governor has done with the Readiness Project and the Governor's Education Action Agenda (*see Appendix #2*), the Commission acknowledges that, in the next

couple of years the Commonwealth's top priority will necessarily be preserving the existing level of quality in our public education system. The Commission determined that the state's greatest near-term opportunity is to seize this moment to make some significant changes in the structure, operating assumptions and delivery mechanisms that comprise our system of public education. In the long run, the Commission concluded that the state's strategy for educational transformation must make efficiencies and restructuring a part of genuine education reform. As these changes are implemented, any available revenues can then be directed to the education sector in the knowledge that they will be spent efficiently and effectively.

This report presents the Commission's recommendations on cost-savings measures and revenue options. Where the report indicates that the Commission "recommends" a particular approach, it means that the prevailing but not unanimous opinion of the diverse Commission is implied. The cost-saving strategies are discussed in detail, leading with the Commission's recommendations and followed by other ideas that were presented by the task forces but not discussed in depth by the Commission. Additionally, the Commission's discussions on revenues are outlined.

Background on the Commission

The Commission, chaired by Gloria Larson, President of Bentley University, and John Fish, CEO of Suffolk Construction, consisted of business, education, labor and policy leaders (*see Appendix #1 for a list of members*). To support the Commission's work, Secretary of Education Paul Reville and the Executive Office of Education enlisted the assistance of expert consultants and created three task forces to examine each of the sectors in public education: early education and care, K-12 and higher education. The task forces and consultants were charged with presenting facts and proposals that would facilitate discussion among Commission members about methods of financing public education. The Commission was also briefed by the Executive Office for Administration and Finance on the state of education funding in the Commonwealth and on the state budget's long-term structural imbalance.

The Commission's Deliberations

Members examined various proposals during the course of seven working meetings and one public hearing. They offered candid reactions, expressed their views freely and tabled political considerations. As a result, discussions were direct and wide-ranging. At the same time, shared principles among Commission members provided a foundation for their deliberations.

First, Commission members agreed that any cost savings achieved through their recommendations should be retained in the field of education and directly benefit the local communities and schools in which savings would be realized. For example, if a municipality moves its employees into the Group Insurance Commission to garner better health insurance rates, savings from such a decision should accrue to the municipality with schools benefiting proportionately.

Second, Commission members agreed that existing tax dollars must be spent efficiently before taxpayers are asked to bear additional burdens. To that end, the Commission supported the idea of linking increments of state aid to the implementation of certain cost-savings ideas. Aid could be withheld or added to encourage particular practices that are sensible, consistent with statewide goals and ultimately beneficial to students.

For example, a service delivery strategy for early education providers or a group purchasing policy for higher education institutions could be required before state aid is issued to those entities. In the realm of K-12, the state could require municipalities to accomplish some percentage of the menu of cost-savings measures proposed in this report (e.g., moving retirees into Medicare) before receiving their full allotment of Chapter 70 aid. A positive side effect of such an approach is that practices once viewed as politically difficult become more feasible when state aid is the incentive. At the same time, the Commission acknowledged that municipalities and districts must be given the tools necessary to implement these changes before this kind of linkage is established.

Finally, members noted that funding for existing institutions and practices is already regarded by some as inadequate and growing more so with each passing year. This is especially the case in light of rising health care and transportation costs, which consume any inflation-indexed increases in annual state aid. They acknowledged the tension between financing existing systems of education and constructing a new, 21st century system. They also recognized that the needs of the present compete with the needs of the future in a time of scarce resources.

Despite these challenges, Commission members agreed that standing still is not an option. The current economic climate only heightens the need to facilitate the best possible educational opportunities for all children, and seeds of reform are grown in moments of crisis. With that in mind, the Commission presents its cost-savings ideas and recommendations.

Opportunities for Cost Savings

The Commission found that Massachusetts' education delivery system suffers from a variety of inefficiencies and came to widespread agreement on six areas in which schools, municipalities and the Commonwealth should seek to achieve significant cost savings. Therefore, the Commission recommends:

1. Reducing municipal employee health insurance costs by moving municipalities into the Group Insurance Commission (GIC) or programs with equivalent or better rates and enabling this action by granting plan design authority to municipal managers;
2. Reducing retiree benefit costs by moving retired teachers into Medicare;
3. Increasing efficiency and capacity through regionalization;
4. Maximizing federal Medicaid reimbursements for special education costs and exploring other avenues to reduce or spread costs.
5. Reducing procurement costs through procurement reform, enhanced use of collaboratives and coordinated purchasing; and
6. Reducing energy costs through the use of energy savings companies (ESCOs), conservation campaigns and better purchasing.

The Need for Revenue

Many Commission members strongly expressed the view that new investment would be required to fund current and future education reforms. Commission members urged, however, that any changes in revenue policy should be carefully employed so as to avoid negatively impacting the state's economic competitiveness. At the same time, many Commission members highlighted the fact that prudent investment in the state's education delivery system is a fundamental and proven method of economic development.

Commission members were determined both to be responsive to the immediate fiscal crisis and to maintain a focus on long-term strategy. In this context, many Commission members argued for a balanced, multi-pronged approach of requiring cost-cutting and efficiency strategies along with educational reform and revenue measures. It was acknowledged that such an approach might require concessions from multiple constituencies. However, Commission members firmly believed that these efforts both to reform education and to implement the Readiness Project are vital, and that the Commonwealth must make continuing, appropriate investments to guarantee our success in the future and our competitiveness on an increasingly competitive, global stage.

II. COST SAVINGS AND EFFICIENCIES

The Commission was presented with an extensive list of cost-savings and efficiencies proposals created by the three task forces and the Public Consulting Group (*see Appendix #9 for a comprehensive list*). Over the course of their deliberations the Commission focused on those areas in which they collectively saw the most potential. Based upon those discussions, the Commission is presenting six recommendations, which are described below.

In addition to the Commission's recommendations, information and ideas that emerged from the work of the three cost-savings task forces are included in the descriptions below. They provide valuable context and insights, and are supplementary to the six main recommendations of the Commission.

Reducing Health Insurance Costs

- ***The Commission recommends reducing health insurance costs by moving municipalities into the Group Insurance Commission (GIC) or programs with equivalent or better rates. In order to enable these changes, the Commission also recommends giving municipal managers plan design authority.***

The Commission found that health care is the number one driver of increased costs in municipal budgets and that significant savings can be achieved in the area of procuring health insurance. Moving municipal employees into the Group Insurance Commission (GIC) is one method of containing costs because the GIC's rates, as a result of its significant purchasing power, have increased at substantially lower rates than municipal health plan rates. Commission members also noted, however, that viable alternatives exist. For some municipalities the GIC may not offer the best deal. Consequently, the Commission recommends that municipalities join the GIC or a program with equivalent or better rates.

Commission members also noted that municipal managers have a difficult time finding significant cost savings because health insurance plan design (i.e., determining benefits, co-pays and deductibles) is part of the collective bargaining process. As a result, the Commission recommends removing plan design decisions from this process. It was noted that, in many circumstances, unions oppose this recommendation. It was also observed that it is essential to provide plan design

authority to municipal managers if the state is going to tie any form of state education aid to a municipality's implementation of cost savings strategies in the realm of health insurance.

Between \$75 and \$125 million of savings on behalf of school employees and retirees might be saved if the Commission's health insurance recommendations were adopted. Total school and non-school savings could amount to between \$100 and \$200 million dollars. These savings estimates are uncertain partly due to data limitations and partly due to behavioral factors that may erode the savings for cities and towns.

Reducing the Cost of Retiree Benefits

- ***The Commission recommends reducing retiree benefit costs by moving retired teachers into Medicare.***

The Commission recommends that municipalities adopt existing statutory provisions to move their eligible retired teachers into the federal Medicare program (via Massachusetts General Laws Chapter 32B, Section 18 or the newly enacted Section 18A). Currently, if a municipality's employees are not in Medicare or the GIC's retired Municipal Teacher Program, the municipality contracts with a health insurance provider through a group plan with their active employees. While the benefits of such programs can sometimes be marginally more generous, the costs are far higher than the plans provided by the GIC and Medicare. It was noted that, to the extent retirees' costs go up as a result of this change, one approach would be to share the savings found at the municipal level with the impacted retirees.

Some Commission members suggested strengthening this provision by urging the Legislature to pass a law requiring municipalities to enroll their retirees in Medicare rather than leaving it as a local option.

If municipalities move their eligible retired teachers into Medicare, total savings of roughly \$135 million could be realized. The majority of these savings, approximately \$115 million, would accrue to cities and towns that have not yet adopted Section 18, and the remaining \$20 million in savings would accrue to their retired teachers.

Increasing Efficiency and Capacity Through Regionalization

- ***The Commission recommends increasing efficiency and capacity through regionalization.***

The Commission generally endorsed the Readiness Project's call for reducing the number of school districts in the K-12 system in order to achieve efficiencies, build capacity and extend the reach of limited resources. The Commission also supported the idea of greater regional collaboration in both higher education and early childhood education as well.

The ability to achieve efficiencies and economies of scale through regionalization and centralized management and service delivery was highlighted consistently during presentations to the Commission. Commission members noted the tension between greater centralization and the

state's own strong tradition of local control. They also acknowledged the educational benefits of school autonomy. At the same time, it was largely agreed that the luxury of autonomy is too expensive under current fiscal circumstances.

Commission members recognized that the timeframe required to consolidate districts would not be conducive to realizing near-term cost savings and efficiencies. However, it was argued that economies of scale and local autonomy can be reconciled with each other to a limited degree if the primary thrust of initial regionalization or district consolidation efforts is confined to "back-office" functions. In this context, it was noted that communities care a great deal about local control of their teachers and curriculum but such concern does not extend to more administrative and operational areas, including food services, transportation contracts and building maintenance.

Because consolidating back-office functions is significantly less controversial than full district consolidation, there is an opportunity to achieve efficiencies in these areas in an accelerated timeframe, and the benefits can apply in and between all three sectors of education. For example, the early education and care task force estimated that centralizing responsibilities such as billing, human resources, staffing services and marketing could yield more than \$1,000 per child.

The Executive Office of Education estimates that regionalization of districts under 1,500 pupils could save a small district close to \$150,000 on bureaucratic expenses, which would result in a total of nearly \$20 million in savings throughout the Commonwealth. The 134 school districts in Massachusetts with fewer than 1,500 pupils spend, on average, just over 36 percent of their budgets on bureaucratic expenses such as central office administration, operations and maintenance, insurance, and out-of-district expenses. In contrast, the 151 districts in the Commonwealth which enroll between 1,501 and 5,000 pupils spend, on average, 34.5 percent of their budgets on bureaucratic expenses. Districts with fewer than 1,500 pupils have average total school budgets of \$10 million, so each district might capture up to \$150,000 in savings on bureaucratic expenses. Alternatively, districts might choose to reallocate these savings to student-centered services that directly impact the experience of children in classrooms.

Reducing Special Education Costs

- ***The Commission recommends maximizing federal Medicaid reimbursements for special education costs and exploring other avenues to reduce or spread costs.***

The Commission recommends that the state work with school districts to maximize federal Medicaid reimbursements for special education costs, which are significant due to the state's higher-than-average special education population. Of the 939,806 students enrolled in Massachusetts public K-12 in 2006-07, 159,757 students, or approximately 17%, were enrolled in special education services. The national average is 13%.

The Commission also observed that, in fiscal year 2007, Massachusetts school districts spent more than \$1.7 billion dollars in direct costs to provide special education services, which represented 16.9% of the statewide education budget. This compares with a national average of 13% of spending for special education services. Additionally, special education transportation was

repeatedly cited as representing a major portion of municipal budgets and, therefore, an opportunity for reform.

With these statistics in mind, the Commission identified three existing revenue sources in which there is potential for growth.

- *Medicaid billing for public school health services* – Massachusetts school districts currently bill for more than \$100 million dollars annually for eligible federal Medicaid health services provided in public school settings. The Commonwealth is currently in negotiations with the Centers for Medicare and Medicaid Services (CMS) for approval of a Medicaid State Plan Amendment which will implement new coverage and reimbursement methodology for school health services, moving from a “per diem” model to a “fee-for-service” model. Numerous states have implemented this new methodology, resulting in reimbursement increases of 20% to 100%. By one estimate, if such a change is made, Massachusetts could increase its statewide reimbursements by \$10 to \$50 million dollars.
- *Medicaid billing for private special education “Chapter 766” schools* – Cities and towns place complex-needs students in licensed group care facilities known as “Chapter 766 Schools,” and some of these schools have cost-sharing agreements with Massachusetts public agencies such as the Department of Mental Health, the Department of Mental Retardation, the Department of Social Services and the Department of Youth Services. Currently, municipalities are billing the federal government \$15 million dollars annually for these students. An estimated range of \$25 million to \$55 million dollars could be available if cost determination and cost sharing agreements are standardized.
- *Accessing dollars from private insurers by increasing the types of medical diagnoses they must cover* – The Commission noted a recent *Boston Globe* article highlighting a national effort by “Autism Speaks” for private insurance to cover intensive, expensive educational treatments (The *Boston Globe*, Push on for Insurers to Share Autism Costs, Erica Noonan, September 16, 2008). Private insurance companies have long contested that they are precluded from covering health services provided in school settings because the cost of this service is covered by the child’s right to a “free and appropriate education” under federal special education law. The Commission noted that state law could be changed to require that private insurers cover more diagnoses, which would help cover the high cost of special education services in the state. However, some Commission members objected to such a change, arguing that new mandates could undercut the state’s efforts to control costs as part of health care reform.

Addressing Underclaiming of Federal Reimbursements

The K-12 task force noted that there appears to be significant underclaiming of federal Medicaid reimbursements because the incentives are not in place for school districts to fill out the necessary paperwork. The early education task force identified this as an area for review, with an emphasis on reimbursements for children’s mental health services. One of the main reasons for underclaiming identified by early education providers is the lack of capacity to apply for Medicaid reimbursements. Another is the fact that reimbursements often do not flow to the entity that makes the claim.

The K-12 task force also noted that Medicaid reimbursements to districts could be increased by revising the state law that currently sends reimbursements into the municipality's general fund and not to the school district (Massachusetts General Laws, Chapter 44, Section 72). The task force highlighted the Town of Milton's "home rule petition" from July of 2008 that supersedes state law and requires all Medicaid reimbursement funds to go to a separate account controlled by the school committee. As a result, there is more incentive for Milton schools to apply for and thereby maximize reimbursements.

The task force also presented the idea that the state could follow this example to increase federal Medicaid reimbursements by working with the Massachusetts Municipal Association to increase the percentage of money that cities and towns share with districts, or by passing legislation allocating Medicaid reimbursement to public school budgets. It was noted, however, that a majority of municipalities already use Medicaid reimbursements from the local general fund to fund schools' "net school spending" requirements. In some cases, then, transfer of reimbursements to school committees would merely result in a shift in control of revenue and not an increase in spending on schools.

Therefore, in order to effectively incentivize the claiming of these reimbursements, any movement towards giving Medicaid revenues directly to schools needs to be carefully structured. As the issue of increasing access to these federal dollars is reviewed, the task forces highlighted the importance of simultaneously involving municipal officials, public and private early childhood providers and K-12 district officials.

Reducing Procurement Costs

- ***The Commission recommends reducing procurement costs through enhanced use of collaboratives, coordinated purchasing and procurement reform.***

Enhanced Use of Collaboratives

As various notions of regionalization and centralization of services become more developed, the Commission recommends that an effective first step would be to ensure the quality of, promote and better utilize collaboratives. Members see opportunity for savings through the increased use, improvement and expansion of the existing collaborative infrastructure. In this context the K-12 task force suggested that an accreditation process for collaboratives would serve to improve the quality of services.

In Massachusetts, there are currently 29 educational collaboratives that provide a host of inter-district support services to nearly 300 member school systems. Collaboratives provide services in the areas of cooperative purchasing, management support, student transportation, research, technology development, implementation of health and safety programs and professional development.

As a means of promoting collaboratives the K-12 task force noted that the state could mandate that clusters of school districts with very low student enrollments use collaboratives for providing regional operational services such as purchasing, transportation and food service. The task force's

research showed that the states of Connecticut and Washington use educational collaboratives particularly effectively and the task force suggests that Massachusetts could consider adopting the best practices from those and other states.

The task force also observed that collaboratives can facilitate the use of cost-effective services in the areas of staffing and professional development, including mentoring and induction; bulk purchasing, transportation planning and delivery; more special education placements rather than private placements, using student outcomes as part of the determination criteria; technology planning, installation and maintenance; energy management; and data collection, reporting and analysis.

Finally, the task force suggested merging smaller collaboratives into larger collaboratives or networking them into existing ones. In order to create more demand for collaboratives that provide high-quality, cost-effective services, the task force noted that one way would be to establish financial and non-financial incentives for using collaborative services.

Coordinated Purchasing and Procurement Reform

The Commission recommends that each of the three sectors adopt methods of coordinated purchasing and procurement both system-wide and potentially across systems. The task forces noted that eligible early education and care providers, K-12 schools and all public institutions of higher education could purchase certain items from one state bid/contract list (or through the state's Comm-PASS program), which would result in lowered costs. The K-12 task force also presented the idea of allowing educational collaboratives to make purchases from a vendor's contract that has been competitively procured by out-of-state collaboratives or out-of-state municipalities.

Commission members widely agreed that efficiencies could be achieved by updating the state's procurement law (Massachusetts General Law Chapter 30B). Raising the amounts above which a municipality must solicit bids through a formal, multi-week bid process would facilitate increased bidding by phone, saving time and paper. In the same realm, the K-12 task force suggested that allowing more market-responsive purchasing practices by accredited purchasing agents would result in a more efficient process. This task force also noted that the state contract system (Comm-PASS) sometimes does not provide the most competitive price and recommends creating an internet-based library or repository of quality bid documents for major purchases. Lastly, in order to capitalize on the procurement technology and resources that currently exist, the task force proposed increasing the amount of purchasing training that school district administrators receive.

Similarly, in the area of procurement, the higher education task force provided several examples of cost-savings opportunities. This task force argued that public institutions of higher education ought to examine group purchasing in the following areas:

- *Energy/Utilities (gas, electric, oil and water)* – The higher education task force felt strongly that this area represents the potential for the highest amount of savings system-wide. In addition to joint contracting that would reduce costs, the task force suggested that there is the potential to develop joint ventures with energy savings

companies that could ultimately reduce consumption, lower costs and reduce higher education's carbon footprint.

- *Bookstore Contracts* – The nine state colleges have a single contract that has been extremely beneficial and financially rewarding.
- *Banking Contracts* – In 2005 three of the six CONNECT Partnership campuses bid a joint banking contract resulting in a net savings of \$100,000. In addition, the campuses saw a marked increase in the quality and range of services provided.
- *Financial Audit Services* – The task force noted that securing a statewide contract for required annual auditing would result in lower costs, standardized methodology and high quality service. This would also allow for the ability to easily aggregate financial information about the system.
- *Office Supplies* – For each of the public campuses, the expenditures for office supplies represent a large portion of non-salary budgets, and acquisition of one system-wide contract would generate significant savings for each campus.
- *Food Services* – Each of the 29 public campuses contracts with a food service vendor, and while some campuses have the same vendor, there are currently no joint contracts.
- *Waste Management* – The amount of trash and recyclable materials on each of the 29 campuses is staggering. A joint review of processing methodologies and joint contracting has the potential to minimize the environmental impact of waste and to reduce costs for processing.
- *Technology* – Annual expenditures by campuses and students constitute a major technology investment worth millions of dollars, and the task force suggested that important savings could be realized with a single contract.
- *Vending Contracts* – Commissions and cash contributions provided to the campuses through snack and soft drink vending contracts are significant. The task force noted that creating a single contract apportioned to each campus could potentially increase revenue and investments for all colleges.
- *Copy Machines* – The task force observed that joint bidding for copy machines could increase the quality of equipment and reduce costs at the same time.

Reducing Energy Costs

- ***The Commission recommends reducing energy costs through the use of energy savings companies (ESCOs), conservation campaigns and better purchasing.***

The Commission found that creating energy savings companies (ESCOs) among schools, municipal buildings, public colleges and others could lead to substantial savings. The K-12 task force noted that municipalities and districts could engage in energy savings campaigns both internally and with external partners, including gas and electric companies. It was observed that some schools have already arranged such deals, reaping rewards for shedding electrical loads during high demand periods.

Additionally, the Commission noted that the use of ESCOs as a model to achieve energy savings can be applied across multiple sectors. These contracts with utility companies have yielded substantial savings to many institutional customers. The task forces noted, for example, that public and private early childhood providers could collaborate with each other and potentially partner with entities in K-12 and higher education to achieve these savings.

In 2005-2006, for example, the town of Belmont installed energy conservation measures in six schools and five town buildings under a 10-year energy savings performance contract. As a result, \$1.7 million dollars worth of improvements are being funded from the annual savings that will be generated by the measures. Additionally, Springfield, Quincy, Belmont, Mount Wachusett Community College, and towns and regional school districts in Franklin County have all undertaken, or are in the midst of, ESCO-funded energy savings projects with contract terms extending between 10 and 20 years.

By one estimate annual savings in this realm for K-12 schools could range from \$36 to \$72 million dollars, and total municipal savings (including the K-12 savings) could range from \$59 to \$107 million dollars, inclusive of savings from projects already undertaken or underway. Additionally, a key advantage of using ESCOs is the ability to finance energy measures without using existing revenues or adding to bonded debt.

III. REVENUE DISCUSSIONS

The Commission determined that the Readiness Project is a priority initiative for the Commonwealth that deserves support and investment, and that cost savings alone will not be sufficient to facilitate meaningful progress in this bold education reform. Given the budget deficit, the importance of protecting existing education services and the goal of moving forward with Readiness Project initiatives, many Commission members felt that additional funds are necessary. In this context Commission members emphasized that any revenue-generating measures should be tied inextricably to restructuring measures intended to realize cost savings and efficiencies.

The Commission broadly discussed a variety of revenue measures, including the sales tax, the gas tax, the income tax, interest and dividends taxes and the licensing of casinos. Based on an analysis reported to the Commission by Augenblick, Palaich and Associates, Inc. (APA) (*see Appendix #7*), the Commission learned that the tax burden in Massachusetts is lower than that of most nearby states and about the same as a handful of states that are similarly situated in terms of population, wealth and student education needs. Additionally, APA reported to the Commission that the overall tax burden in Massachusetts has decreased significantly since 1995, and the reductions were generally greater than those in other states over the same time period.

The Commission discussed the sales tax as the most viable option, noting that – as currently structured – it is relatively progressive and less volatile than income tax revenues. While there was discussion about the merits of broadening the base of the sales tax, some of the statutory exemptions such as food and clothing items up to \$175 were highlighted as being worthwhile and important to maintain. Additionally, the Commission learned that increasing the sales tax from the current rate of 5% to 6% is estimated to result in approximately \$720 million dollars in new revenue. Commission members agreed that, if this tax were to be increased, some or all of the new dollars should be dedicated to education needs.

Commission members discussed the merits of increasing the gas tax and acknowledged that, while an attractive opportunity, it is perceived that any increase would likely be devoted to transportation-related projects. Commission members also discussed the income tax, noting that it is the single largest source of revenue for the state. The Commission also considered the rate at which interest and dividends are taxed. However, Commission members generally saw these as less tenable approaches given the need to balance any new revenue measures with the state's ability to remain economically competitive.

Outside of the traditional forms of state revenue, the Commission encouraged the use of private fundraising as a means for jumpstarting the Governor's education agenda. It was noted that the Executive Office of Education is currently planning to raise private money to support planning grants for Readiness Schools and Readiness Centers. Commission members noted that private fundraising operates as a way of giving donors a crucial stake in public education. In this context, the business community will also be afforded the opportunity to become an increasingly active and fully invested partner in education reform, and to directly impact the Commonwealth's future workforce. This strategic and leveraged investment will directly impact our ability to compete in a global economy.

Finally, Commission members felt strongly that, even if it were feasible to immediately implement all of the cost-savings strategies outlined in this report, increased funding would still be necessary to develop and sustain a high-performance education system. Because of these considerations and the interest in presenting a long-term, sustainable solution, the Commission acknowledged that new revenues will be needed and that some portion of any new revenues ought to be dedicated to the education sector.

IV. CONCLUSION

The Readiness Finance Commission members agreed that the education sector needs to be a top priority for the state, and represents a worthwhile, indeed critical, investment for the long-term growth and success of the Commonwealth. The Commission recognized that, in this nearly unprecedented fiscal downturn, there is both a need to facilitate the maintenance of basic services and an opportunity to pursue cost-savings strategies and efficiency-related reforms. Commission members also stressed the importance of continuing to make progress on the Governor's Education Action agenda to achieve a 21st century education system.

Commission members agreed that, in order to accomplish these goals, implementation of the cost-savings and efficiency-related strategies described in this report should begin immediately. Many Commission members felt that additional funds will be necessary to maintain basic educational services and to pursue future Readiness initiatives, and that these initiatives represent a vital investment. However, to guarantee the most cost-effective and efficient use of taxpayer dollars, many Commission members also emphasized that any new revenue-generating measures should be tied simultaneously to the bold restructuring and reforms detailed in this report and in the Readiness Project.

LIST OF APPENDICES

Appendix 1:

List: Readiness Finance Commission Members

Appendix 2:

Background on the Readiness Project

Appendix 3:

Strategic Education Initiatives

Appendix 4:

- a. Snapshot of Public Consulting Group's Analysis
- b. Background on the Department of Early Education and Care
- c.** Other Cost Savings Proposals Presented by the Task Forces
- d.** Other Revenue-Related Ideas

Appendix 5:

Report: "Current Status of State Budget" by the Executive Office for Administration and Finance

Appendix 6:

Report: "Elementary and Secondary Education Cost Analysis and Recommendations" by the Public Consulting Group

Appendix 7:

Report: "Comparative Analysis: Massachusetts Tax Study" by Augenblick, Palaich & Associates

Appendix 8:

Slides: "Funding Challenges in Current Educational Programs" by Cam Huff and Ed Moscovitch

Appendix 9:

List: "Comprehensive List of Cost Savings and Efficiencies Proposals" by Cam Huff

APPENDIX #1 – MEMBERS OF THE READINESS FINANCE COMMISSION

John Fish	President and CEO	Suffolk Construction Company
Gloria Larson	President	Bentley University
Jose Alvarez	President and CEO	Stop & Shop
Chris Anderson	President	Massachusetts High Technology Council
Senator Robert Antonioni	State Senator	Massachusetts State Senate
Jeffrey Bussgang	General Partner	Flybridge Capital Partners
James Caradonio	Superintendent	Worcester Public Schools
Jack Connors	Founding Partner and Chairman	Hill, Holliday, Connors, Cosmopolos
Mayor Kim Driscoll	Mayor	Salem, Massachusetts
Mark Edwards	Managing Partner	Edwards & Company
Michael Flynn	2008 Teacher of the Year	Southampton Public Schools
Representative Patricia Haddad	State Representative	Massachusetts House of Representatives
John Hamill	Chairman of the Board	Sovereign Bank
Jackie Jenkins-Scott	President	Wheelock College
Wendell Knox	President and CEO	Abt Associates Inc.
Grace Lee	First Deputy Treasurer/General Counsel	Office of the State Treasurer
Lisa Lynch	Dean and Professor of Economics	Brandeis University
Karen Hawley Miles	Executive Director	Education Resource Strategies
Tom Payzant	Professor	Harvard Graduate School of Education
Marta Rosa	Director, Government Affairs/ Senior Interim Director	Wheelock College
Joe Tucci	President and CEO	EMC Corporation
Michael Widmer	President	Massachusetts Taxpayers Foundation
Anne Wass	President	Massachusetts Teachers Association

APPENDIX #2 – BACKGROUND ON THE READINESS PROJECT

In June of 2007, Governor Patrick created the Readiness Project Leadership Council and charged it with developing ideas that would transform public education in Massachusetts over the next decade. Their recommendations – the culmination of subcommittee meetings, public hearings, town halls with the Governor and extensive research – led to the Governor’s Education Action Agenda, a comprehensive blueprint that offers every student, at every point on the learning spectrum, an opportunity to become highly educated and fully prepared for the 21st century.

Building on the success of the past 15 years of education reform, the Governor’s Action Agenda seeks to address the disconnect between the demands of today’s fast-paced, technology-driven society and public education’s outdated, outmoded structure; it seeks to close, once and for all, the pernicious achievement gap for minority students; and it seeks to make what students learn more relevant and responsive to the world and the economy in which they will build productive adult lives. The achievement of these goals is critical to individual success, but it is equally as important to the state’s overall economic competitiveness and civic vitality.

The Governor’s Action Agenda, aimed at high achievement for all, has two major themes: (1) the improvement of teaching and learning in every pre-K through graduate level classroom in the Commonwealth; and (2) the provision of health and human service supports; expanded learning time opportunities; and pre-school, after school and summer programs so that each child can come to school genuinely ready to learn.

Thoughtful, realistic, well-timed action steps that are taken over the next decade offer the way ahead for Massachusetts education reform. They include:

- Increased support for early childhood education and care, with the goal of achieving universal pre-kindergarten;
- Early intervention and language development programs for low-income children ages 18 months to three years;
- At least two years of community college for all students, beginning with a targeted approach;
- A school day and a school year that is structured to match the demands of students, teachers and families;
- The establishment of Readiness Schools, which will replicate the best practices of pilot and charter schools in school districts around the state;
- The creation of a robust educator development system; and
- The integration of 21st century skills into all aspects of public education.

The Governor’s vision has attracted the support of educators, business leaders, students and families, many of whom participated in the Readiness Project as part of its Leadership Council, 13 subcommittees and countless gatherings, large and small. With their help, steps are already being taken: Universal pre-kindergarten is now a reality in more cities and towns. Expanded learning time exists in more schools. And the state recently made an historic investment in higher education capital construction. The Governor is committed, in spite of current fiscal challenges, to move forward on the implementation of this bold vision of a high-performing, 21st century school system.

APPENDIX #3 – STRATEGIC EDUCATION INITIATIVES

FY10 Budget

Unless there is a continuing and steep decline in revenue projections, Secretary Reville and the Executive Office of Education intend to recommend the following Readiness items for modest expansion in the fiscal year 2010 budget.

- ***Birth to School Age:*** This program provides intensive, home-based language and literacy in high-priority school districts (as defined by the Department of Elementary and Secondary Education) and helps reach our youngest and most vulnerable children, including homeless children. The Commonwealth's investment in assisting low-income parents in developing their children's language capacity must be expanded.
- ***Universal Pre-Kindergarten:*** The goal with this account is to begin building a high quality, comprehensive UPK system (rather than a program) in Massachusetts. The system will be dedicated to providing excellence, parent access and affordability. Increased investment will depend on funding, and access will depend on adjustments to the levels of income-eligibility.
- ***Expanded Learning Time:*** The ELT program provides funds for districts to extend their school day for approximately 10 per hours per week or two hours per day. This allows schools to expand their academic offerings throughout each day, and preliminary evidence suggests this strategy helps to reduce the achievement gap. The program currently serves 13,500 students in 26 public schools and is regarded as the leading national pilot program in this field. Modest expansion of the program to a few additional schools and districts will be sought.
- ***Chapter 70 Increase:*** The goal of the Chapter 70 aid distribution is to ensure that – through an equitable combination of local property taxes and state aid – every K-12 district has sufficient resources to meet its foundation budget spending level. Some increase in Chapter 70 aid will be essential for districts to sustain services and undertake reforms. Chapter 70 aid represents approximately 14% of the state budget.
- ***Increased Financial Aid:*** Financial aid plays a significant role in providing access to post-secondary education. The Commonwealth's funding of student financial aid, however, has declined at a time when student charges and enrollments have been increasing at the Commonwealth's public institutions of higher education. This trend is particularly evident in the MASSGrant account, the Commonwealth's core need-based financial aid program, which can be used by needy students to cover student charges at both public and private colleges in the Commonwealth. Demand for public higher education is increasing dramatically and financial aid must increase correspondingly.
- ***Free Community College:*** The fiscal year 2010 free community college account is intended to fund the first phase of a comprehensive program to provide all full- and part-time degree and certificate-seeking students enrolled in a public community college in the Commonwealth with financial aid equal to the difference between the student's direct costs (tuition, fees, books and supplies, and health insurance) and the amount of federal and state grant/categorical aid the student may be eligible to receive, such as Pell Grants, MASSGrants, and tuition and fee waivers. This first installment of "free community college" would be offered exclusively to teachers and potential teachers in the early

education and care system and to low-income parents of children in the public education system.

Longer Term Costs/Expansions

The following is a sample list of estimated cost projections for several of the Readiness Project's key agenda items. This is a partial list. These cost estimates are contingent upon numerous intermediary policy decisions which would affect the scope of services provided.

- ***Universal Pre-Kindergarten:*** \$302 million if eligibility level is set at 50% of area median income; and \$595 million if eligibility level is set at 85% of area median income
- ***Full-Day Kindergarten:*** \$2.7 million extends full-day kindergarten to all high-needs districts and allows districts that did not initially receive transition funds to receive quality improvement grants
- ***Expanded Learning Time:*** \$219 million serves all "Commissioner's Districts," as defined by the Department of Elementary and Secondary Education (i.e., 9 high-needs urban districts)
- ***Free Community College:*** \$92 million serves all 51,000 full and part-time students in the community college system
- ***Increased Financial Aid:*** \$29 million restores MassGrants to fiscal year 1989 peak

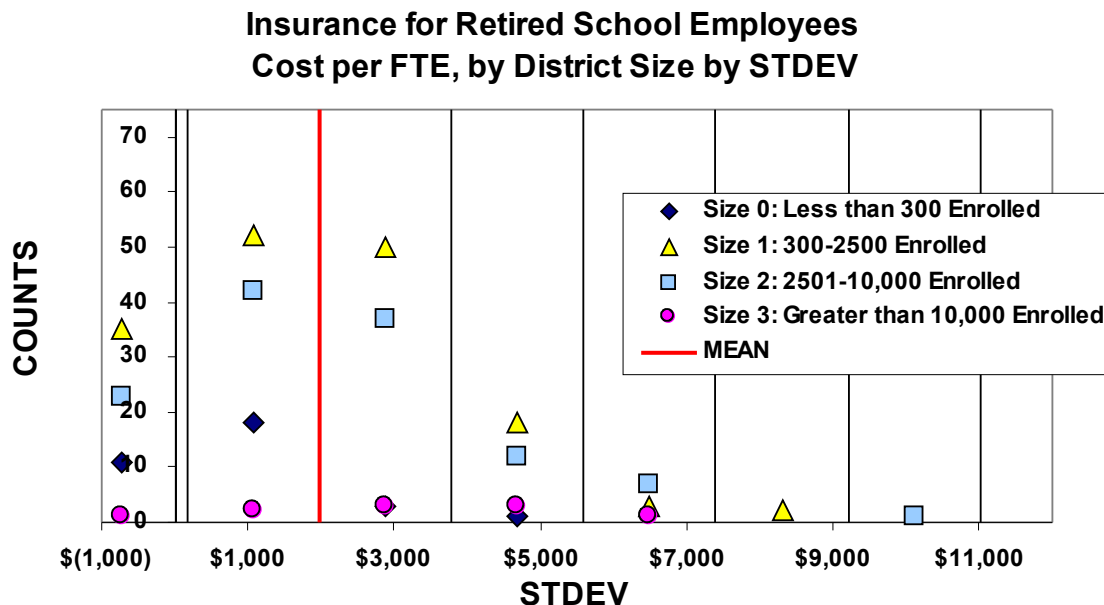
APPENDIX #4 – SNAPSHOT OF PCG ANALYSIS; BACKGROUND ON THE DEPARTMENT OF EARLY EDUCATION AND CARE; OTHER COST-SAVINGS PROPOSALS; AND OTHER REVENUE-RELATED IDEAS

A. SNAPSHOT OF PUBLIC CONSULTING GROUP'S ANALYSIS

The Public Consulting Group (PCG) analyzed Massachusetts elementary and secondary education spending using the most recent data available, from 2006-2007 (*see Appendix #6 for full report*). PCG assessed district expenditures in tiers by relative size, and across categories ranging from administrative and teaching to utility and heating costs. They then identified potential areas for cost savings, increased operational efficiency and revenue generation.

In its presentation, PCG detailed the results of its analysis of current spending in K-12 that compared the average unit cost of service for every major category of school spending across the state with the average unit cost in each school district. They then calculated the potential savings in each spending category if expenditures in high-cost districts were brought down to within one standard deviation of the statewide average. Finally, PCG explained how spending in those districts might be reduced, as well as how statewide average costs in several spending areas could be lowered.

Below is an example of the expenditure analysis done by PCG:



PCG also analyzed the expenditure categories and sub-categories of the foundation budget and determined that the greatest impact could be made in the areas of administration, instructional leadership, pupil services, professional development, operations and management, insurance, retirement programs and other benefits and payments to out-of-district special education schools.

Broadly, PCG proposes rethinking the business model used by districts and making system changes in order to reduce costs in these areas. PCG's research revealed that district expenditures were highly variable across the categories of superintendents, professional development, legal services and building and curriculum leadership.

In the area of commodity purchasing, PCG proposed reducing costs by improving purchasing in the most highly variable expenditure categories of transportation, heating/utilities and health insurance for retired and active employees. In this last area, PCG found that, between 2001 and 2006, municipal health insurance costs rose by almost 92%, while the state's health insurance costs rose by 48%. Additionally, Massachusetts ranked second in the nation in the cost of its benefits for school employees in fiscal year 2006. PCG found that a number of factors contribute to high spending, including larger than market reliance on indemnity plans, lower contribution rates for employees and smaller purchasing risk pools.

B. BACKGROUND ON THE DEPARTMENT OF EARLY EDUCATION AND CARE

Because it is relatively new as a cohesive sector and operates in a different manner than the rest of our education delivery system, a brief primer on the Department of Early Education and Care (EEC) is warranted. EEC was established in 2005 to create a coordinated, comprehensive system of early education and after-school programming in Massachusetts – resulting in the first Department of Early Education and Care in the country. It is a growing sector, as evidenced by the size of the waiting list, and it is widely acknowledged as an excellent investment and a leading priority for Governor Patrick and the Legislature.

EEC is more than 96% federally funded or matched, and its administrative costs are 1.7% of its total budget. It licenses and monitors the operations of 12,000 early education, child care and after-school providers statewide, serving approximately 275,000 children from birth through age 14 every day. EEC also provides financial assistance to low-income and at-risk families, serving more than 72,000 children. Lastly, it provides resource, referral and family support for families across the state.

EEC currently purchases multiple services through a range of methods. Financial assistance to parents is managed through three mechanisms: grants to Community Partnerships for Children (CPCs), who administer them locally; vouchers, which are administered regionally through the Child Care Resource and Referrals (CCR&Rs); and direct contracts between EEC and providers. The service delivery system currently includes: approximately \$14 million dollars for CPCs, approximately \$10 million dollars for CCR&Rs, approximately \$30 million dollars for Family Child Care Systems, \$5.4 million dollars for Massachusetts Family Networks and \$60,000 for Early Childhood Resource Centers.

Currently, approximately 18,000 children are on EEC's waiting list. Eliminating the waiting list would cost approximately \$35 million dollars for pre-school alone. Notably, of EEC's \$579.7 million dollar budget in fiscal year 2009, all but \$21.3 million dollars includes and leverages federal funds. Consequently, the early education task force noted that any opportunity for and method of cost savings must protect against loss of federal funding.

The EEC task force noted that several economists and experts have concluded that there is a significant return on investment for making high-quality early education programs available to all children in Massachusetts. The task force explained that reliable, quality early education and care arrangements lead to reduced employee turnover, lowered absenteeism, increased productivity and positive business relationships. They also noted that low-income children who participate in high-quality early childhood education are 40% less likely to need special education or be held back a grade, 30% more likely to graduate from high school and twice as likely to go to college.

C. OTHER COST SAVINGS PROPOSALS PRESENTED BY THE TASK FORCES

Special Education:

- Provide early, intensive, instructional interventions which will lower referrals to special education
- Modify the special education circuit breaker by providing financial incentives for both in-district or collaborative placements, rather than more costly private placements
- Audit district budgets spent on out-of-district special education placements and require action plans to provide more in-district and/or collaborative placements
- Use local collaboratives to provide more programs and special education transportation
- Analyze and change the state's tuition setting processes for private special education schools
- Address changing levels of service after students are admitted at Chapter 766 Private Special Education schools, which result in increased costs. Require that, once a student is admitted to a Chapter 766 school, his/her charges can be adjusted only for inflation or for a mutually agreed-upon increase in service level based on the determination of the district and the parents, not on the determination of the 766 school.
- Revise the process for allocating paraprofessionals to special education classes. According to the task force, the State of Illinois determines student-to-teacher ratios based on grade level and disability categories. By contrast, in Massachusetts the current student-to-teacher ratio is categorically 8:1 if no paraprofessional is present and may be a maximum of 12:1 if a paraprofessional is present. The task force observed that there is no research on the effective ratio of paraprofessionals to special needs students and notes that the federal government has no criteria. Consequently, the task force proposes modifying the student-to-teacher ratio requirements more along the lines of those used in the State of Illinois. In this context it was noted that any reform strategy should take into account differing ability levels within a given category.

Demographic Changes

Massachusetts is facing enrollment declines and a demographic shift in its K-12 education workforce that should result in potential cost reductions over the next five years. Data suggest that a "retirement bubble" is approaching. PCG's research shows that 29% percent of teachers are older than age 54, 17% of teachers are between the ages of 54 and 58 and the average age of teacher retirement is between 58 and 59 nationally. Consequently, PCG pointed out that, as teachers retire and new lower salaried teachers are hired, the potential reduction in costs, also referred to as "turnover savings," could be up to \$400 million dollars per year.

Grants Development and Management

The K-12 task force examined the grant-issuing process used by the Department of Elementary and Secondary Education (ESE) and suggested some revisions. The task force proposed that ESE review the amount of each allocation in proportion to the overall awards issued and that it have the authority to shift under-awarded funds when necessary. The task force also noted that the process could involve an evaluation of outcomes achieved with use of the grant funds.

The task force indicated that grant funding procedures are cumbersome and should be streamlined. In order to make these improvements, the task force proposed encouraging ESE, the Department of Higher Education and other relevant state agencies to offer Joint Requests for Proposals, in which they might match funding, to create partnerships between K-12 and higher education institutions and to distribute funds to and through accredited collaboratives.

Transportation

The K-12 task force observed that transportation, and particularly special education transportation, is increasingly coming to represent a larger and larger share of municipal budgets. To alleviate the burden, the task force presented the possibility that the state might provide districts with internet-based transportation routing software, increase the use of collaboratives to provide regional transportation for students in adjacent districts and update state law for transportation requirements. The task force noted that current transportation requirements deserving review include the distance from home to school, the transport of private and parochial school students and the costs for charter school transportation. Additionally, the task force suggests that a collection of experts in the transportation field be gathered on a pro bono basis to review bus transportation contracts of school districts. The task force proposed that such a group be convened and tasked with issuing detailed recommendations for specific cost-saving actions for both regular and special education students.

Other Ways to Create Immediate Savings

Based on a survey of superintendents in which 117 superintendents responded, the K-12 task force also generated the following list of ways to create immediate savings:

- Put MCAS online and save money for printing and shipping.
- Translate documents into multiple languages one time and establish an internet-based “library” of these documents for all districts to use.
- Provide school committees the flexibility to complete their required hours of instruction (currently 900 hours for elementary schools and 990 hours for secondary schools) in fewer than 180 school days. Some school districts may wish to lengthen the school day and schedule a 4-day school week in order to save on energy and/or transportation costs.
- Allow Licensed Practical Nurses (LPNs) to provide health services in schools. Require LPNs to work under the direct supervision of a certified school nurse. The task force noted that, by using LPNs, as hospitals and clinics do, schools can provide more health care services to children. It was also noted that the work school nurses do helps to lower dropout rates, decrease school absences and keep students ready to learn.
- Require school personnel to develop an Individual Student Success Plan (ISSP) for students who fail to pass the MCAS. Also require school districts to create an Educational Proficiency Plan (EPP) for those students who do not achieve Proficiency on the MCAS.
 - Freeze the requirement to do EPPs, or require the Department of Elementary and Secondary Education to revise the ISSP and include a section for the EPP. (One

document; not two). School personnel will complete the EPP after the Department develops a single “unified” document.

- Give Annual Awards (Governor’s; Secretary of Education’s; Commissioner’s, etc.) for districts that create savings and efficiencies.
- Assist districts in revising their school vacation schedules to conserve heating fuel, thereby leveraging the knowledge that the lowest temperatures annually occur during certain time periods.
- Early Education Physical Space: one of the most significant costs for programs is space and general overhead associated with it
 - Increase use of energy audits
 - Require state to do a facility inventory
 - Create corporate tax incentives
 - Use public schools

Additionally, in the K-12 realm the Commission acknowledged that, as resources become available, the rates that are embedded in the foundation budget need to be reviewed. For this aspect of the discussion the Commission enlisted the assistance of a Technical Advisory Group, which was made up of several individuals with extensive experience in school finance, including state education officials, policy experts, legislative staff and others. The Technical Advisory Group met twice and examined weaknesses in the Chapter 70 school finance formula as well as the adequacy of the foundation budget. The Group considered several ideas, such as the appropriate measures of income and property wealth in the Chapter 70 formula and the merits of full state funding through a statewide property tax. In light of the current economic climate and the consequent downturn in state revenues, the Commission thereafter focused its efforts on more immediately achievable goals in the realm of cost savings and efficiencies, as outlined above.

Finally, in the realm of public higher education, it was noted that there are in many cases low completion rates for the Free Application for Federal Student Aid (FAFSA). By increasing the completion rates among students at the University of Massachusetts, the state colleges and especially at the community colleges, where there are the lowest completion rates, students will be able to access more federal financial assistance. Such a change also prevents the state from leaving money “on the table” and could serve to alleviate some of the funding problems in higher education.

D. OTHER REVENUE-RELATED IDEAS

In addition to the revenue ideas discussed in Appendix 3, the EEC and K-12 Savings Group made their own suggestions, provided below.

Early Education and Care

- Increase revenue from license plate - “Invest in Children” license plate, which currently generates \$300K per year
 - Use for grants to providers – off budget
- Create retained revenue account for licensing fees, which generate \$1M per year

- Recoup parent fees from those who don't pay, up to \$1.5M per year
- Increase use of small business programs (e.g., for for-profit providers) by utilizing the Small Business Administration, Dept. of Labor to offer services for small business
- Maximize benefit from Higher Education Act: federal reauthorization includes early childhood
 - Build partnerships with higher education
- Create a Committee for Economic Development
 - create endowments in partnership with private sector and federal government, which could be used to provide scholarships or financial incentives to providers for improving learning outcomes
 - encourage contributions by matching donations or giving tax credits
- Create a foundation using, as a model, the Minnesota Early Learning Foundation
 - Fundraising goal: \$30M in five years
 - Minnesota's foundation was established in 2005 and raised \$18 million dollars and leveraged major employers such as: Warren Staley, retired CEO of Cargill; Brad Anderson, CEO of Best Buy; Mark Banks, CEO of BCBS of Minnesota; Robert Bruininks, President of the University of Minnesota, and other corporate and philanthropic executives

Elementary and Secondary Education

- Modify ESE's contract with Pearson, the company that provides the Massachusetts Tests for Educator Licensure (MTEL), to share a percentage of the profits from the sale of MTEL tests
 - Use this money to support teacher mentoring and induction
- Activate the Commonwealth Education Innovation Fund and bring on a high-profile "volunteer" to do fundraising
- Develop a fund to increase planning and implementation to increase use of collaboratives
- Provide additional tax incentives to companies that donate state-of-the art computer equipment to public schools and/or public colleges
 - Encourage schools and colleges to provide some of the funding.
- Increase individual and corporate tax incentives for donations that:
 - serve high percentages of low-income students
 - reduce the achievement gap among student sub-groups
 - increase graduation rates among potential and/or former dropouts
 - help parents/guardians access ESL classes
 - serve both college and K-12 students
- Fund a Performance-Based Award program for school teams that demonstrate continuous improvement in increasing student achievement indicators